DP WORLD

TRADE IN TRANSITION

EXECUTIVE SUMMARY

WRITTEN BY

The Economist INTELLIGENCE UNIT

About this research

Trade in Transition is a global research programme led by The Economist Intelligence Unit, sponsored by DP World, which presents private-sector sentiment on international trade. In this year's report, we specifically explore the impact of covid-19 on companies' trade operations and the resulting shift in approach to international trade by private-sector firms.

The research is based on two global surveys of senior executives involved in their firms' day-to-day international trade decisions and transactions. The first survey of 3,000 respondents was conducted between January and March 2020 and the second survey of 800 respondents was conducted between October and November 2020. Both surveys captured perspectives of executives across six regions (North America, South America, Europe, Middle East and Africa, and Asia Pacific). The survey findings were supplemented with in-depth interviews with trade experts and senior executives across regions and sectors.

Harry Broadman of Berkeley Research Group served as an advisor to the Trade in Transition project and has provided feedback on early drafts of this and subsequent reports.

This executive summary was written by
Chris Clague and edited by Siddharth Poddar.

Executive summary

Eight months ago, the world trade outlook for 2020 was worse than grim. The World Trade Organisation (WTO) released a report in April forecasting that, in its worst-case scenario, the pandemic could push trade down by as much as 32% by year's end. It was a striking figure, but also within the bounds of reason. Most of the world's major economies were in lockdowns of varying severity, international travel had come to an almost complete stop and supply chains for essential goods appeared on the edge of collapse.

However, data covering the first few months of the second half of year show the fall off lessening, and a recovery appears underway.[1] As of December 2020, the WTO forecasts a 9.2% annual decline in trade, still a substantial drop, and slightly better than the current EIU forecast of a 10.6% fall, but far from the disaster once feared.

Results of our global survey of 800 senior executives, sponsored by DP World, also support this relative optimism. Fielded in October and November 2020, we asked executives across a range of industries and regions about the pandemic's effects on trade and their business—including changes in their international sales revenue in the first half of 2020 compared to 2019 (see below). It is a supplement to a 3,000-respondent survey fielded over the first quarter of 2020, during the initial stages of the pandemic.

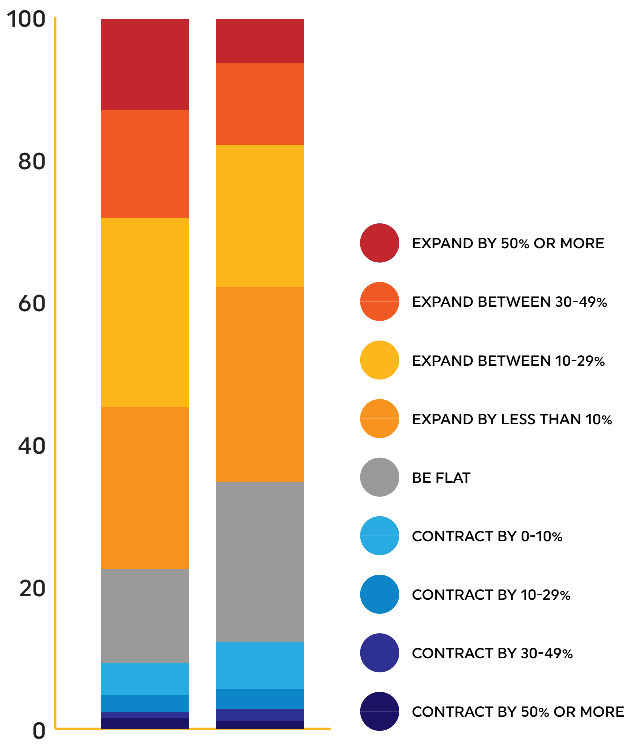
This brief summarises the most recent survey. In early 2021, we will release a series of papers that dive deeper into results from both surveys, highlighting significant sectoral and regional findings.

Great expectations

Our initial survey indicated pre-pandemic expectations for trade for 2020 were strong. Seventy-seven percent of respondents believed their firms' international sales would expand in 2020, with 13% indicating trade would increase by "50% or more" compared to 2019, and an additional 15% expecting trade to rise 30%-49%. Less than 10% of respondents expected a contraction in international trade.

Few, if any, respondents could have known at the time the scope and scale of the crisis the global economy would be soon confronting. Yet for many of them, the pandemic apparently hasn't been so dire, at least insofar as cross-border sales are concerned. Forty-two percent of respondents reported in our second survey that company-wide international revenue expanded in the first half of 2020 and 19% reported no change from the previous year. Thirty-nine percent did report contractions in international sales and although we don't have a metric for comparison, that figure is encouraging at a time when only one of the world's major economies, China, is registering economic growth.

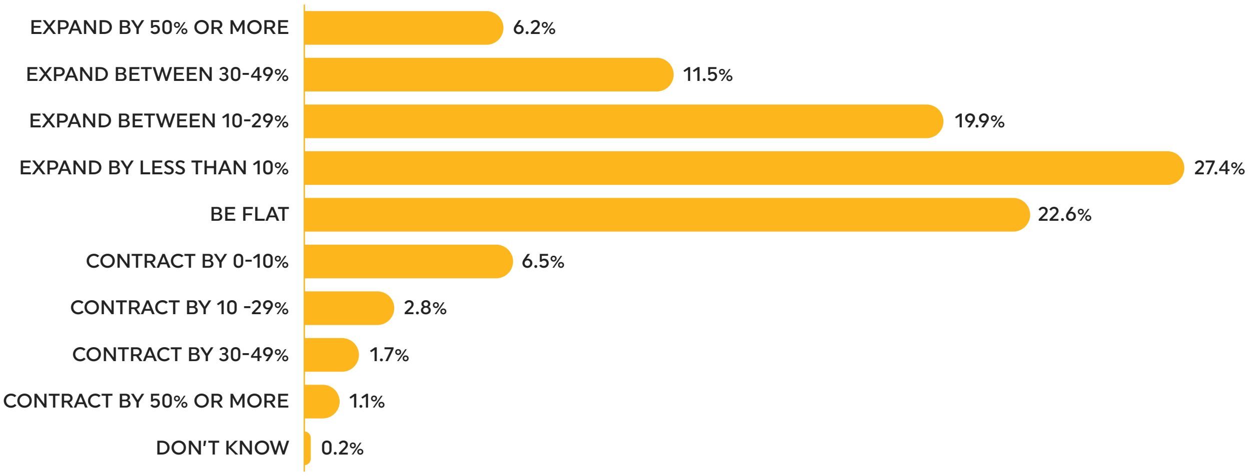
FIGURE 1
From survey conducted in January-March 2020: In 2020, how do you think your firm's international sales revenues and purchases will change compared with 2019?



Source: The Economist Intelligence Unit survey conducted in January-March 2020

[1] See for example: https://unctad.org/system/files/official-document/ditcinf2020d4_en.pdf

FIGURE 2
How much did your firm's international sales revenue change in H1 2020 c ompared with H1 2019? (from survey conducted in October-November 2020)



Source: The Economist Intelligence Unit survey conducted in October-November 2020

Breaking the chains

For at least the past decade, economists, journalists and consultants have been predicting a great shift in global supply chains. It started with the observation that wages were rising on China's eastern seaboard, cutting into the labour-arbitrage play multinational companies had been profiting from even before the country joined the WTO in 2001. With few exceptions, firms opted to absorb the hit to their margins rather than move production elsewhere. Through natural disasters, new trade agreements and newer trade wars, that has more or less remained the case. There has been no great shift.

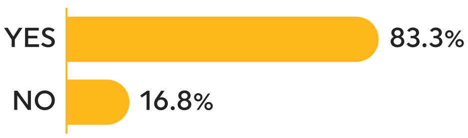
The pandemic might finally be providing the necessary impetus. Eighty-three percent of executives surveyed stated that their firms are "currently in the process of reconfiguring [their] supply chains," which we define as one or more of the following: switching or adding new suppliers, using different logistics providers, and changing production or purchasing locations. A plurality, or even a slim majority, could potentially be dismissed, but when four-fifths of the executives agree, then actual movement is much more likely.

That it's neither a cheap nor an easy task are two reasons why major supply-chain shifts are yet to be evident. However, change appears to be afoot. On average, firms in our survey are reallocating 32% of their revenue from the first half of 2020 to reconfigure their supply chains. Thirty-four percent of respondents are reallocating between 10-29% of revenue, another 30% between 30-40% of revenue, and 22% more than 50%. Considering that companies with more than US$500m in annual revenue comprise half the survey sample size, the sentiment could indicate massive spend in the coming months and years on supply-chain shifts.

One of the more persistent misconceptions about supply chains is that because so many focus on "just in time" delivery, it somehow also means they are easy to move on short notice. This is not the case in most industries. Supply chains are the products of years of investment, relationship-building and education and training, among a host of other factors. They cannot change overnight.

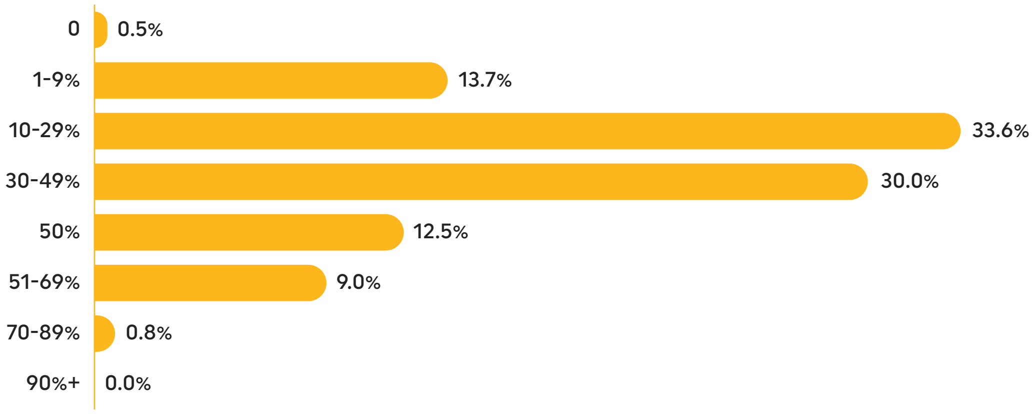
Of the respondents who answered that their firms are reconfiguring their supply chains,

FIGURE 3
Is your firm currently in the process of reconfiguring the most critical parts of your supply chains in response to pandemic-related disruptions?



Source: The Economist Intelligence Unit survey conducted in October-November 2020

FIGURE 4
What percentage of your company's H1 2020 revenues has been re-allocated to reconfiguring your supply chains?



Source: The Economist Intelligence Unit survey conducted in October-November 2020

39% said that the process will take between "6-12 months" and 21% said it would take "longer than a year." By contrast just over 4% said it would take "less than 3 months" and 23% said "3-6 months."

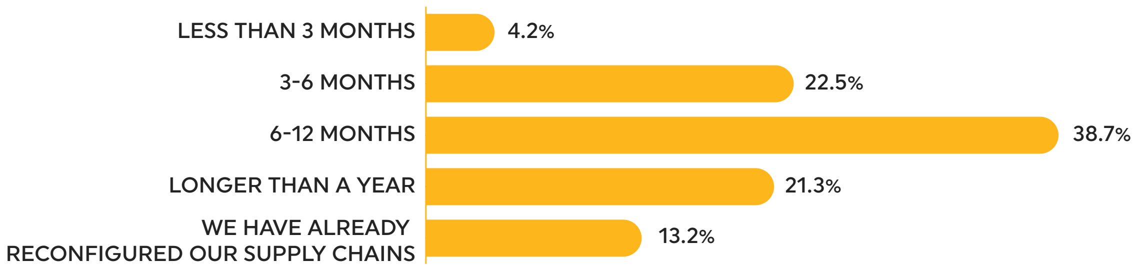
The short(er) road to recovery: GFC vs Covid-19

Over the course of the Global Financial Crisis, from when the value of merchandise trade began trending downward in August 2008, it took just over two years to fully recover, according to the Netherlands Bureau for Economic Policy Analysis' World Trade Monitor, a monthly index of global trade.

More than 70% of respondents to our survey believe trade will recover from the effects of the pandemic in even less time. [2] Asked how long it will take for global trade to return to the same level as the first half of 2019, before the pandemic hit, nearly 27% answered "6-12 months"; 2% even believe that it will take less than six months. The most common response was "1-2 years," which 43% of respondents selected. Only 8% believe that it will take more than five years and less than 2% believe trade will never recover.

Across sectors, the most optimistic for a quick recovery were consumer goods firms, with 36% of them indicating it would take less than a year. Two of the sectors that showed the most pessimism—those with the highest percentage of respondents answering that a recovery would take more than five years—were health and pharmaceuticals (14%), and IT (11%). This is surprising since both have been at the centre of the pandemic and experiencing substantial growth: health and pharmaceuticals for obvious reasons, and IT because it has enabled companies to continue functioning amidst the lockdowns.

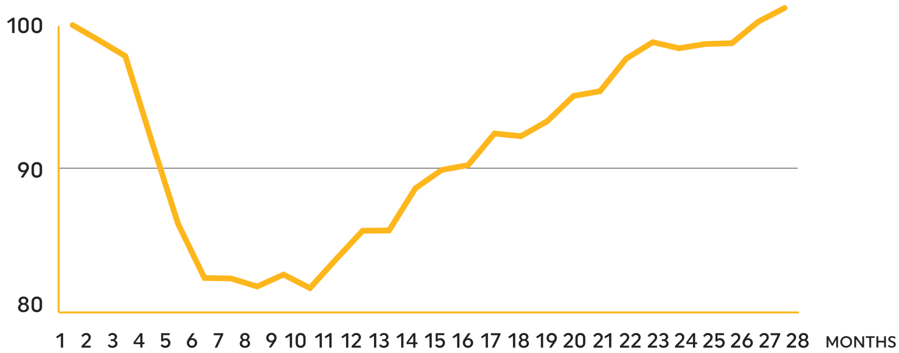
FIGURE 5
How long does your firm estimate it will take to reconfigure your supply chain?



Source: The Economist Intelligence Unit survey conducted in October-November 2020

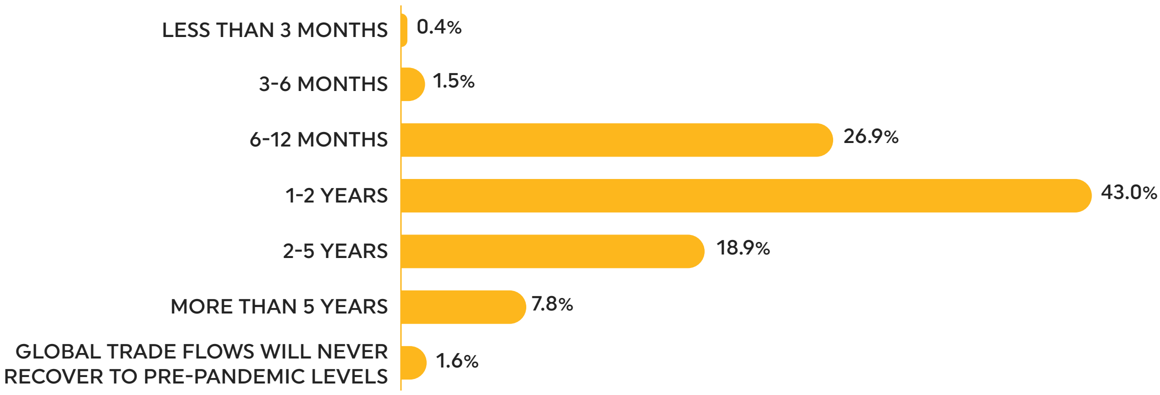
[2] The survey was fielded before the announcements of the viable candidate vaccines.

FIGURE 6
World Trade Monitor (EIU calculations), 2008–2010, months to recovery



Source: CPB Netherlands Bureau for Economic Policy Analysis, The Economist Intelligence Unit

FIGURE 7
How long will it take for world trade flows to return to H1 2019 levels?



Source: The Economist Intelligence Unit survey conducted in October-November 2020

With the exception of construction, energy and natural resources, executives in other sectors—industrials, logistics, transport and travel, and general services—are more hopeful.

Their hope may prove justified. Most cheering for trade perhaps is that starting this week there will be a new administration in the US and while it is likely to bring more of a change in tactics than overall trade strategy, especially regarding China, the world should benefit from a more deliberate, transparent and predictable policymaking process in Washington. In our initial, pre-pandemic survey, "government policy" was selected by the most respondents as the factor that was "most likely to contribute to a contraction in [their] firm's international sales in 2020"—likely stemming from the Trump team's chaotic approach toward trade. More stable global economic leadership from the US should help to ameliorate some of this risk.

That a Brexit deal was also finally agreed in late December also removes the spectre of the UK crashing out of the EU. Neither side got everything it wanted in the agreement, but now that it is in effect (as of January 1st), firms on both sides of the channel—and around the world—can at least begin to make informed decisions about trade and investment.

Still, significant risks to trade remain. The residual effects of import tariffs and export controls imposed on essential goods during the pandemic are likely to continue to weigh on trust between countries, and tensions between the US and China will remain unresolved, particularly in the area of technology.

We will be covering these and other issues in the coming months as we release new reports as part of the *Trade in Transition* series.